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# Structuring Preferential Rights to Purchase in Oil & Gas Transactions: Triggers, Assignment and Enforceability

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Today's faculty features:

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# Structuring Preferential Rights to Purchase in Oil & Gas Transactions:

## Triggers, Assignment and Enforceability

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# I. Introduction

## a. Definition

- i. Gives the holder the right to preempt a contract by matching, within a specific period of time, the terms of a third party' bona fide offer
- ii. Different from an option

## b. Reasons for a preferential right to purchase

- i. Ability to increase interest in desirable property
- ii. Avoid undesirable working interest owners or partners
  - a) Disparity in size of new partner may effectively end the interest of the remaining parties by proposing numerous expensive operations that the remaining parties cannot afford
  - b) Disreputable purchaser
- iii. Avoid third parties getting valuable data gathered during operations

# I. Introduction

- c. Implications for future transactions
  - i. Restraint on transfer not preferred
  - ii. Typical Purchase & Sale Agreement
    - 1) Provide for notice and impact on sale
    - 2) Allocate purchase price to individual properties
    - 3) Obligate buyer to comply if exercise after closing
  - iii. Exists for the duration of the JOA
    - 1) Differs from typical Area of Mutual Interest Agreements
    - 2) Differs from obligation to offer renewed leases

## II. Preferential Rights to Purchase Provisions

- a. Joint Operating Agreements
  - i. Different form agreements, 1956, 1977, 1982
  - ii. 1989 Form
- b. Other agreements
  - i. Purchase and Sale Agreements
  - ii. Plant Ownership Agreements
  - iii. Pipeline Ownership Agreements

# III. What Triggers a Typical Preferential Right to Purchase

- a. Triggers in general
  - i. Bona fide offer that a party decides to accept or has accepted
    - 1) What constitutes a bona fide offer
      - a) Made in good faith
      - b) Is firm - not subject to conditions
    - 2) What type of transfers trigger
      - a) Sale
      - b) Financing arrangements - mezzanine financing
      - c) Involuntary transfers - foreclosure sale or bankruptcy
      - d) Between related entities
      - e) From one co-owner to another
      - f) Mergers or sales of stock
      - g) Non-consent election
      - h) Gift or inheritance

# III. What Triggers a Typical Preferential Right to Purchase

- b. Notice requirements
  - i. Written notice
  - ii. Contents
    - 1) Identity of property
    - 2) Name and address of the purchaser
    - 3) Purchase Price
    - 4) “All other terms of the offer”
  - iii. Insufficient notice
    - 1) Vague notice requirements
    - 2) Effective date of the sale?
    - 3) Obligation of offeree to seek additional terms if desired
- c. Other party in default under the JOA - “suspension of rights”

# IV. Exercising a Preferential Right to Purchase

- a. Time period in which to accept
  - i. JOA - 10 days from receipt of notice
  - ii. In writing
  - iii. Must be unconditional
  - iv. Must accept all terms of the sale
  - v. Extending the time awaiting additional information
- b. Unique consideration
  - i. Stock of the purchasing company
  - ii. Unique property as part of consideration
  - iii. Attempts to thwart a preferential right with unacceptable terms
- c. Property is part of a package sale
  - i. Typical PSA allocates purchase price among property
  - ii. Determination of value in good faith
- d. Multiple parties holding the right
  - i. If some but not all exercise - right to exercise right of declining parties

# V. Remedies for Failure to Provide the Required Notice and Defenses

## a. Remedies

### i. Specific performance

- 1) Preferred remedy
- 2) Must show “ready, willing & able to exercise” right
- 3) Third party must have had notice

### ii. Damages

- 1) Direct - difference between the fair market value and the purchase price
- 2) Consequential - lost revenue from the time of the sale

## b. Defenses

- i. Statute of Frauds, Rule Against Perpetuities
- ii. Limitations, waiver, estoppel, laches

# VI. Assignability of a Preferential Right to Purchase

- a. Personal covenant
  - i. Not assignable
- b. Covenant that runs with the land
  - i. Requirements
    - 1) Parties must have privity of estate
    - 2) Be contained in a grant of land or some interest in land
    - 3) Touch and concern the land
    - 4) Relate to an interest in existence or specifically bind successors
    - 5) Be intended by the original parties to run with the land, and
    - 6) The successor to the burden must have notice of the burden.
  - ii. Binds and is held by successors
    - 1) Issues due to leases held for the long-term

# VII. Drafting Considerations

- a. Limiting the duration of the right
- b. Limiting the assignability of the right
- c. Dealing with unique consideration
- d. Triggering events
  - i. Involuntary transfers
  - ii. Financing arrangements
  - iii. Other
- e. Contents of the notice - “all other terms of the offer”
  - i. Copy of the offer or Purchase and Sale Agreement
- f. Structuring as a “right of first offer”